



Republic of Portugal

Economic Outlook & Debt Management Strategy

January 2011

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I. Economic overview

Key Economic Indicators

In 2009, Portuguese real GDP declined 2.6% (which compares favourably to the Eurozone real GDP decline of 4.1%).

Growth turned positive again in 2010, with the trade balance showing positive dynamics.

The budget deficit is expected to decrease significantly, leading to a slowdown in growth in 2011. However, the trade balance dynamics are set to improve further.

	2009	2010 ^e	2011 ^f
(Rates of change, %)			
Real GDP	-2.6	1.3	0.2
Private Consumption	-1.0	2.0	-0.5
Public Consumption	3.0	1.9	-8.8
Investment (GFCF)	-11.9	-2.0	-2.7
Exports	-11.8	8.6	7.3
Imports	-10.8	6.7	-1.7
Budget Balance (% GDP)	-9.3	-7.3	-4.6
Public Debt (% GDP)	76.1	82.1	86.6
Inflation (a)	-0.8	1.3	2.2
Unemployment Rate	9.5	10.6	10.8

(a) Average annual change

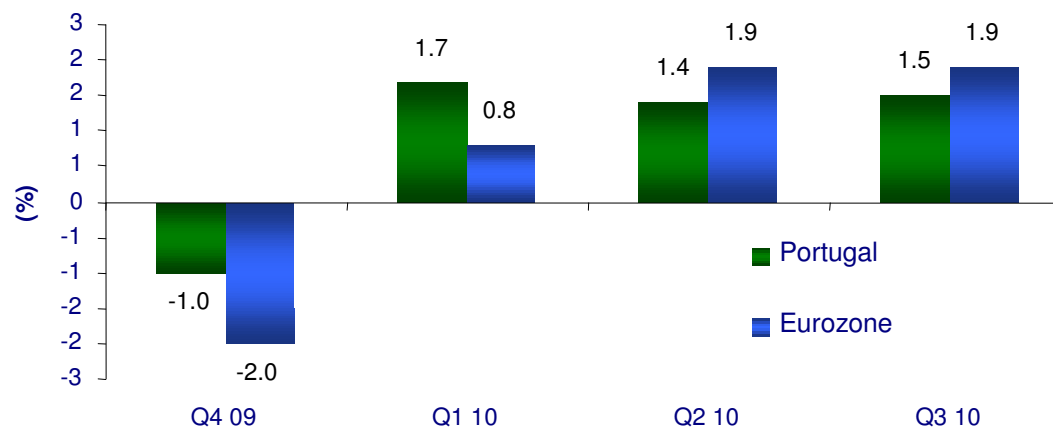
Source: Ministry of Finance and Public Administration

Steering Report on the Budgetary Policy, July 2010 - for 2009 data

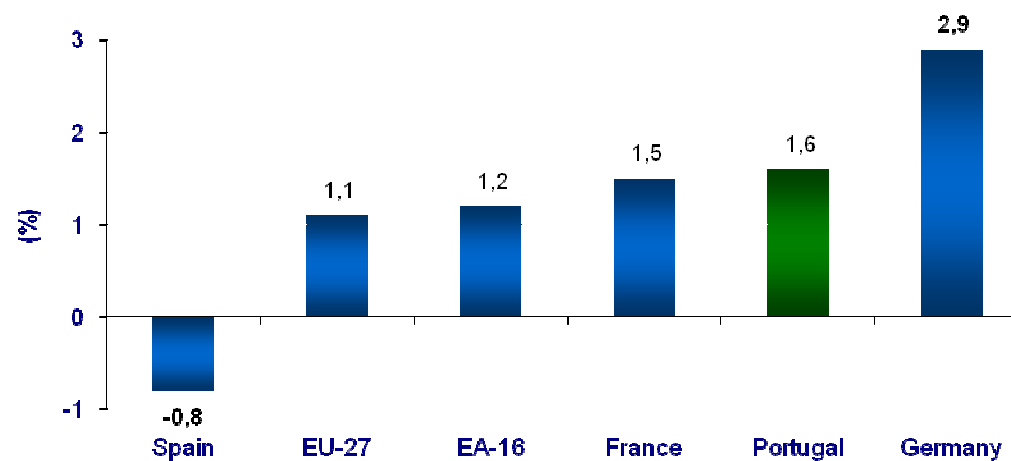
State Budget 2011, Oct 2010 - for 2010 and 2011 data

Economic Growth

Quarterly GDP growth (YoY)



H1 GDP growth (YoY)



The growth rate in Portugal remains positive and above expectations.

Exports remain a key driver for growth:

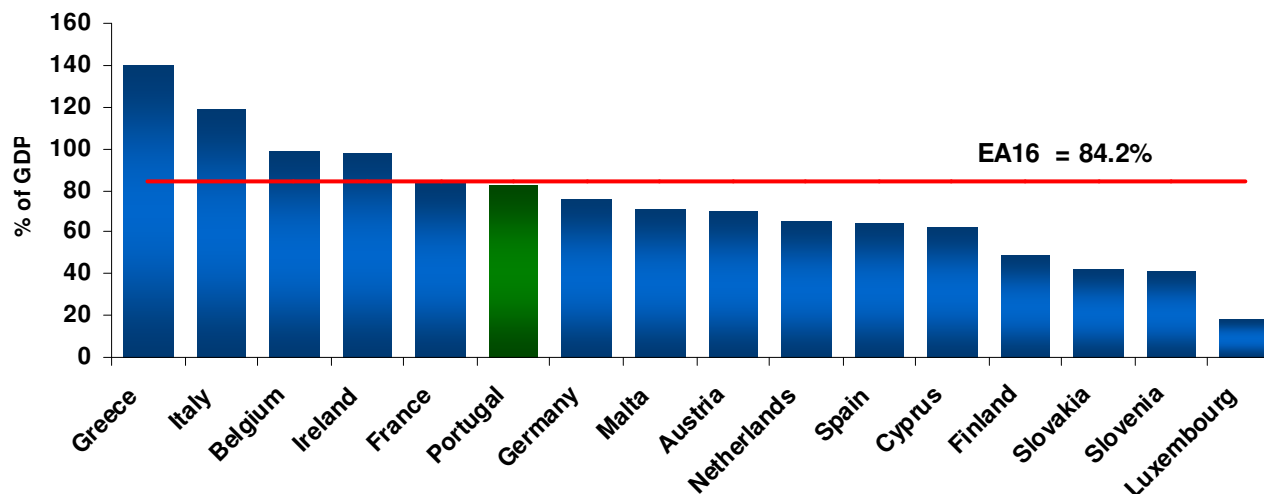
- Exports +14.8% (November YTD)
- Exports to non EU + 16.6% (November YTD)

Public Accounts

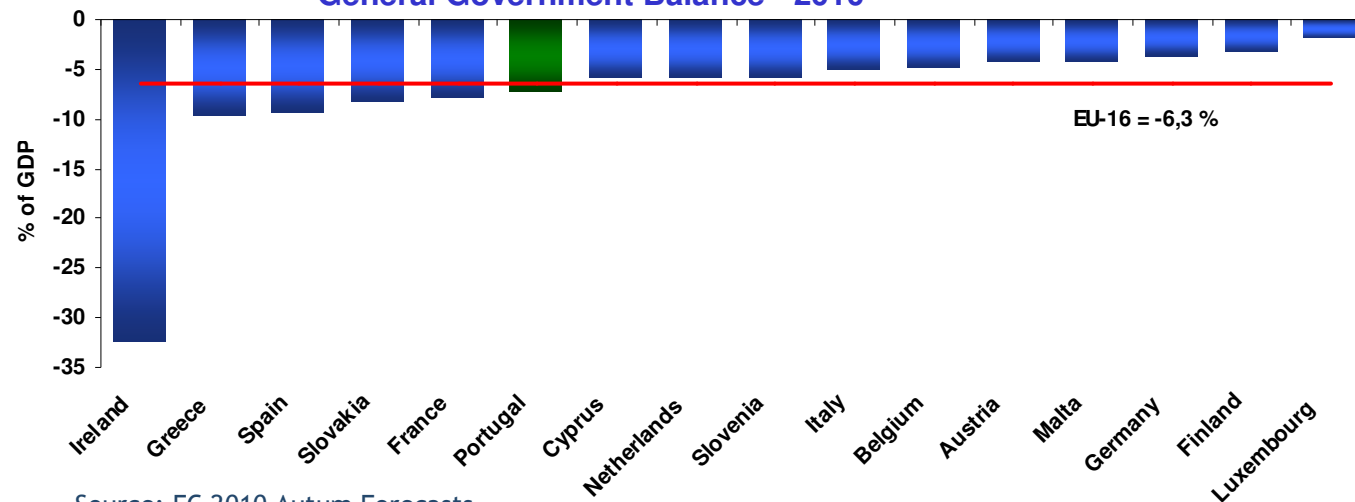
The debt burden is in line with euro area average...

...even if the Portuguese deficit is estimated to be higher than the Euro Area average in 2010.

General Government Debt - 2010



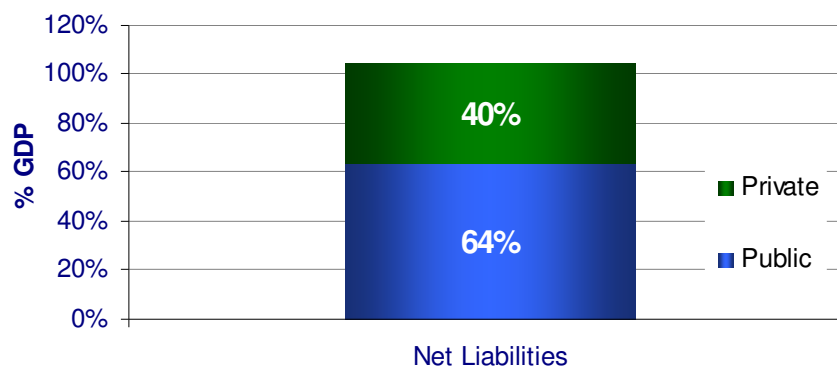
General Government Balance - 2010



Source: EC 2010 Autumn Forecasts

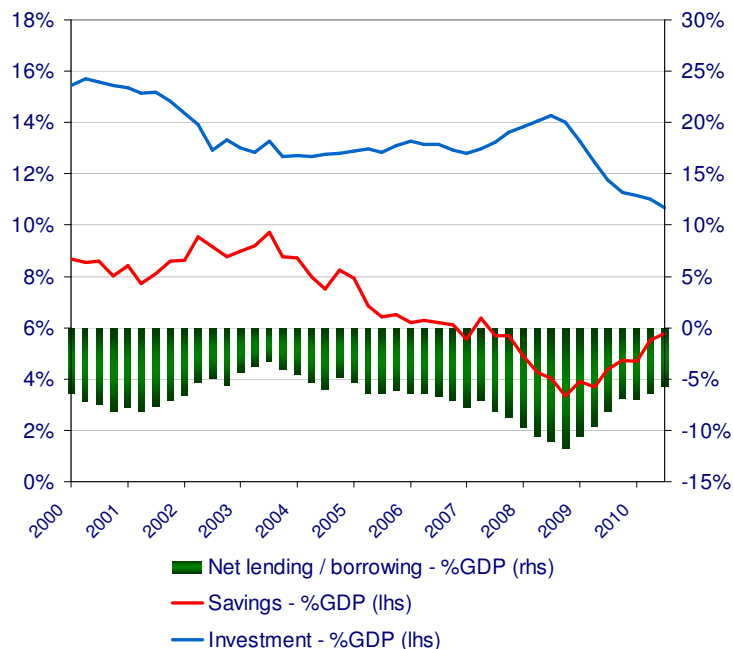
Deleveraging

International Investment Position (Sep 2010)

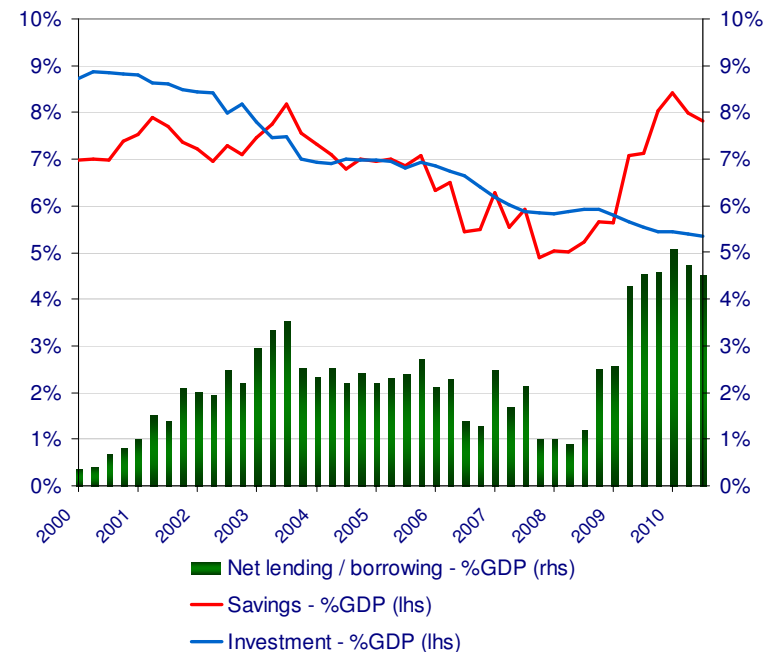


Source: Portuguese Central Bank

Corporates



Households



Source: Statistics Portugal (quarterly data, one-year moving average)

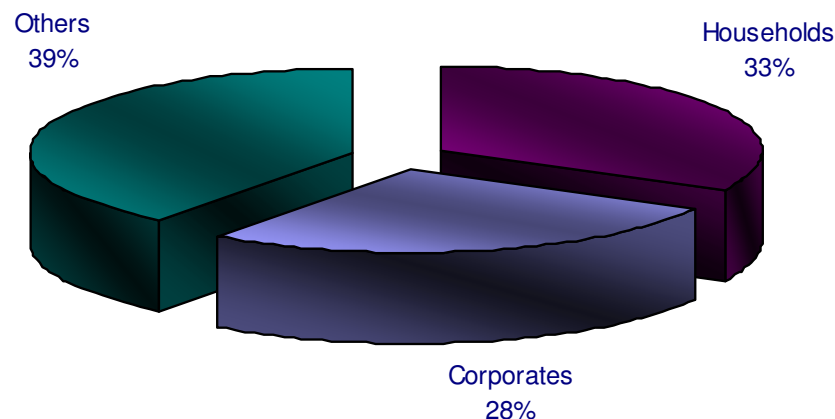
The Portuguese economy has net liabilities amounting to 104% of GDP (as at Sep 2010).

However, the public sector is committed to stabilize its debt levels and...

...as a result of the global credit crunch, there are signs of deleveraging in the private sector.

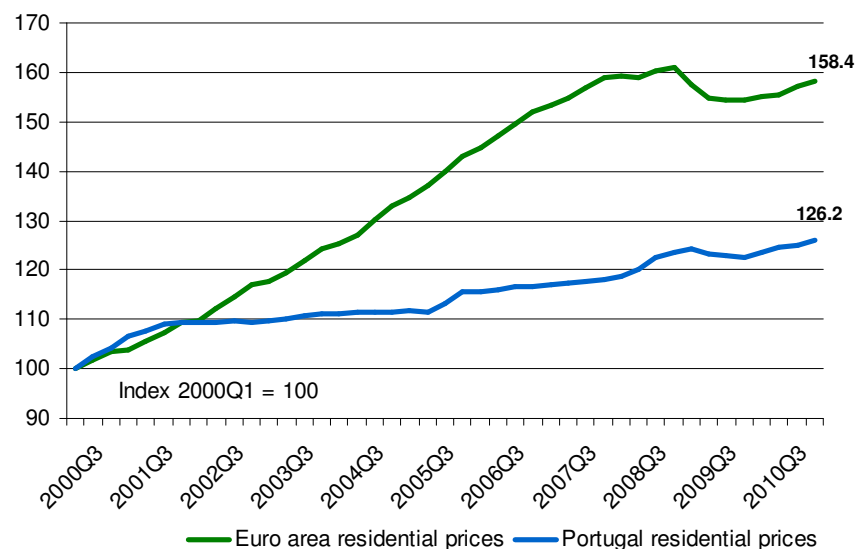
Financial Sector

Credit from Banks (Q2 2010)



Source: Portuguese Central Bank

Residential Prices



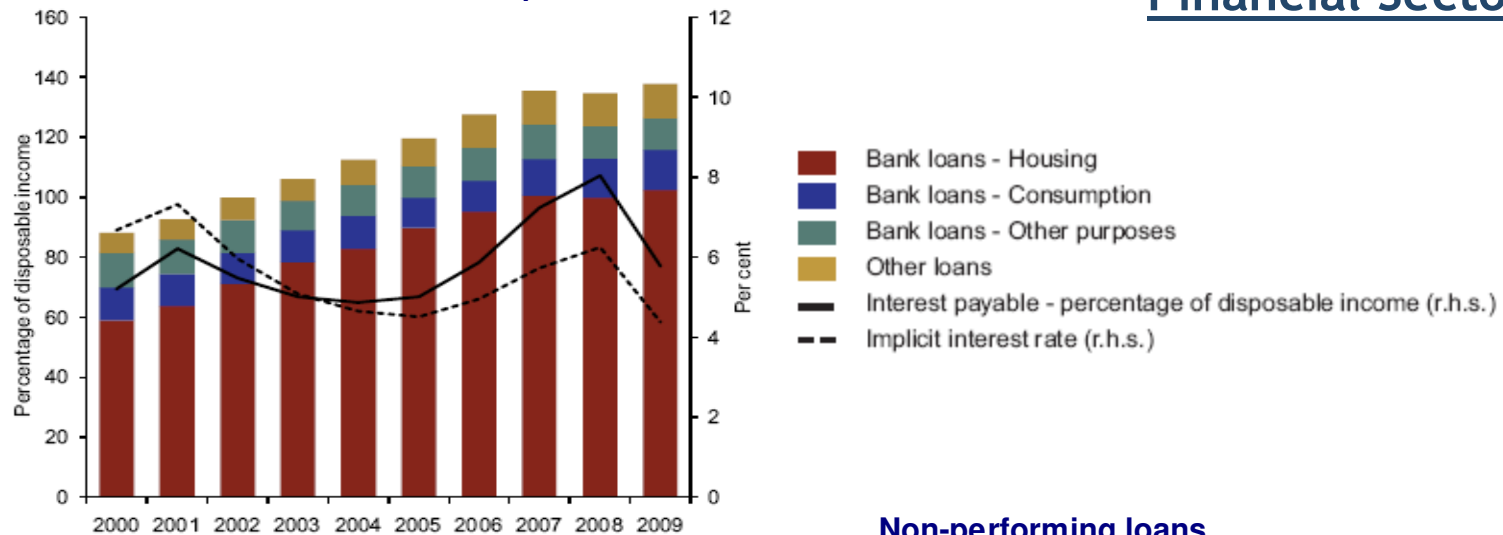
Source: ECB, Eurostat

Portuguese banks business is mainly retail oriented.

The Portuguese financial sector did not suffer a significant impact from the subprime crisis, as a result of a limited exposure to “toxic” assets and the absence of a real estate bubble.

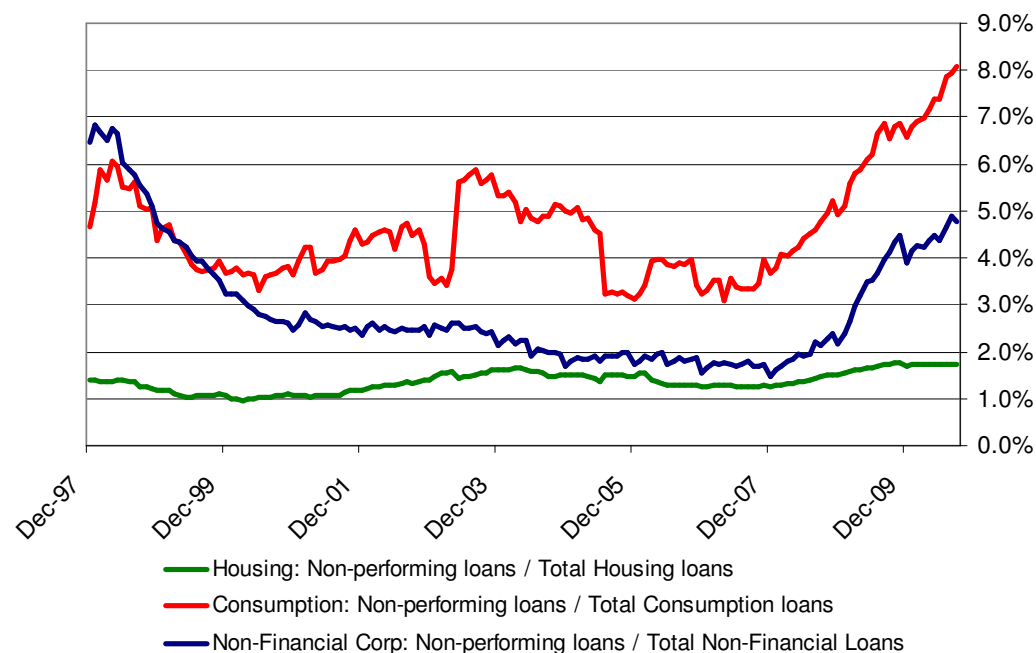
Financial Sector

Household Loans as % of disposable income



Most of the loans outstanding are for housing, which have the lowest non-performing ratios and did not increase substantially during this crisis.

Non-performing loans



Source: Portuguese Central Bank

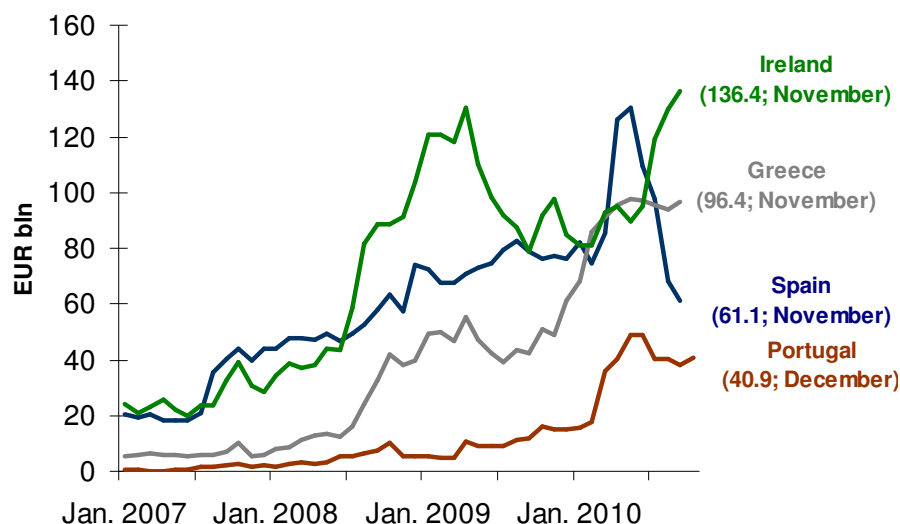
Financial Sector

Portuguese banks' borrowing from the ECB is already showing a downward path.

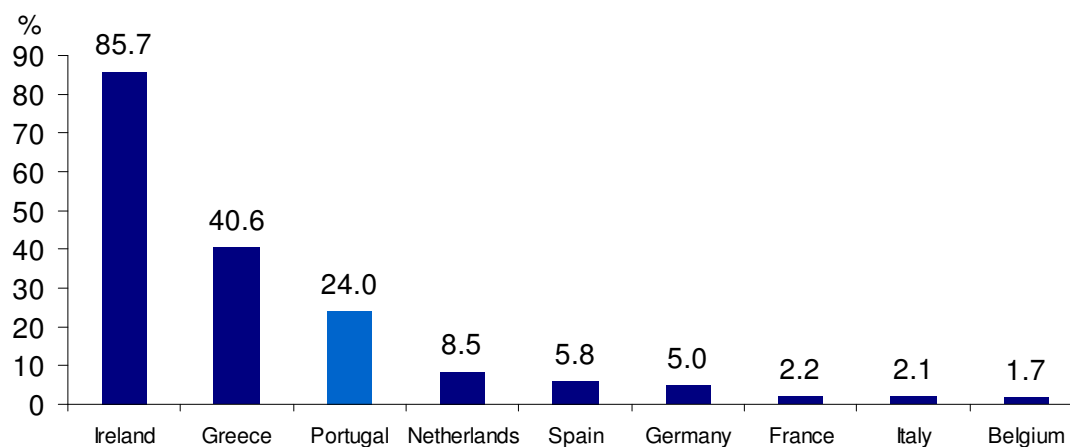
The largest Portuguese banks get on average 60% of their funding from retail clients.

Over 100% on average of their wholesale debt repayment needs in the next three years are covered by eligible assets.

Borrowing from the ECB



Central Bank Liquidity Provision (% GDP)

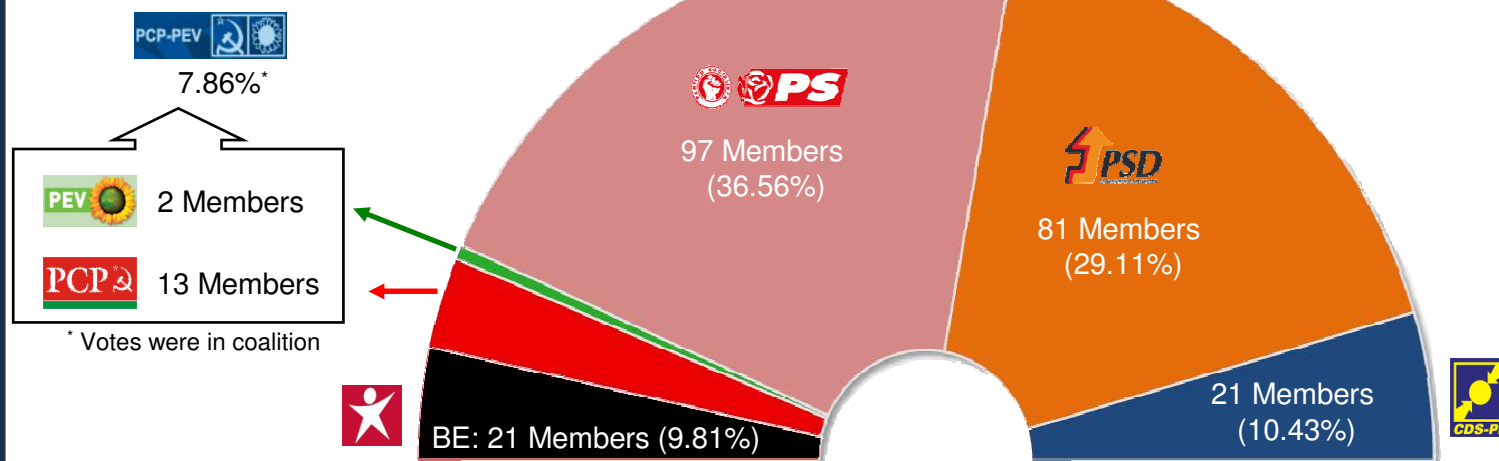


Political & Social Environment

- ✓ The 2011 budget that supports new measures of deficit reduction was approved by the parliament.

Political environment: Clear majority of market friendly parties.

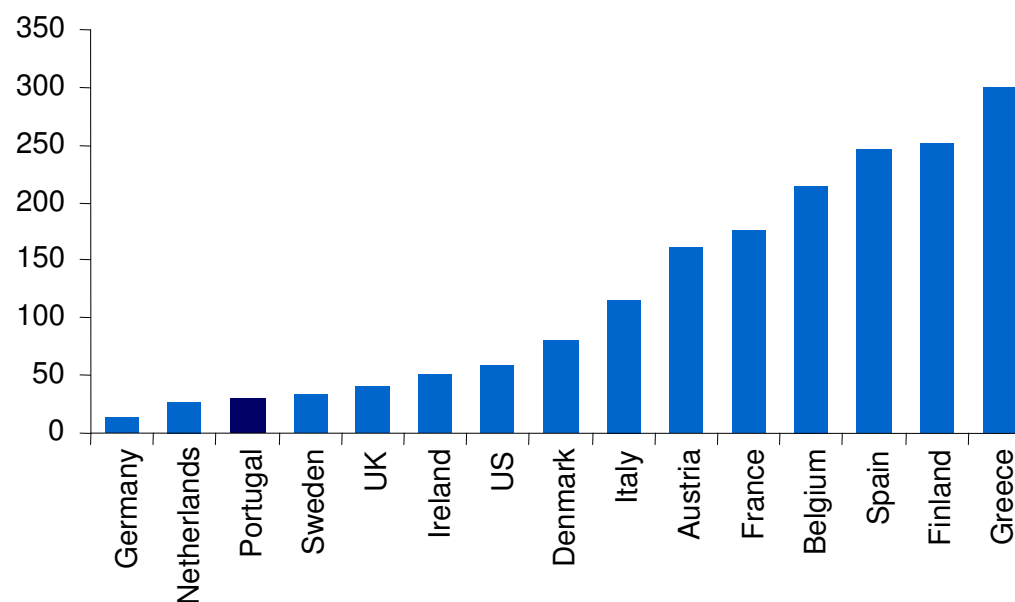
Composition of Parliament and Parliamentary Groups
(Number of MPs by political party and % of total votes, according to the Sep. 2009 General Election)



Political & Social Environment

Above average social cohesion facilitates introduction of austerity measures.

**Number of workdays lost due to strikes*
(per 1000 employees)**



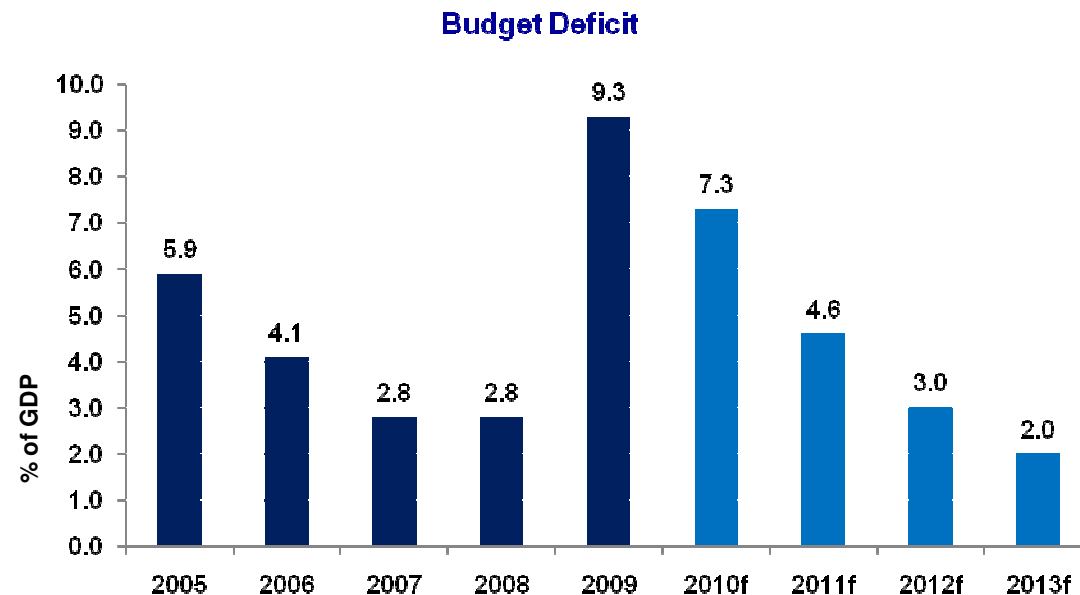
Source: ES Research, Pordata
* 2000-2007 averages, except Greece (1991-2000 average)

II. Recent developments in Public Finances

Budget Deficit

There is a strong political consensus between the two main parties on the need for consolidation of public accounts, and Portugal has already showed signs of the strength of its commitment in the past.

The previous consolidation process was complemented with a social security reform that will improve the sustainability of the public accounts in the long run.



Source: Steering Report on the Budgetary Policy, July 2010

- ✓ The Portuguese PM stated, on Jan 11th, that the preliminary numbers available show that the Portuguese government will not only meet its budget target of 7.3% in 2010, but it will come clearly below that figure

Main Measures for the State Budget for 2011 and for the strengthening of budget execution for 2010

✓ Expenditure cuts - impact of 2.7% of GDP

- 5% overall average reduction on public sector salaries;
- Freeze pensions;
- Reduce travel allowances, overtime expenditure, and elimination of accumulation of public salaries with pensions granted by the public pension system;
- Reduce expenditure with National Health Service (NHS);
- 20% reduction on expenditure with Social Integration Subsidies;
- Reduce public investment on central administration programmes;
- 20% reduction on expenditure with central administration vehicles;
- Extinction/merger of bodies of the public administration;
- Reorganisation and rationalisation of the public companies

The budget for 2011 includes severe austerity measures.

Main Measures for the State Budget for 2011 and for the strengthening of budget execution for 2010

Deficit to GDP targets of 7.3% in 2010 and 4.6% in 2011 were reaffirmed.

- ✓ **Reduction of fiscal expenditure** - impact of 0.4% of GDP
 - Reduction of tax allowances and benefits on Personal Income Tax
 - Review of fiscal benefits on Corporate Income Tax
 - Convergence of tax rates for workers and pension beneficiaries
- ✓ **Increase of fiscal revenue** - impact of 0.6% of GDP
 - 2 p.p. increase on the standard VAT rate (21% to 23%)
 - Levy to the financial system, in line with the ongoing EU initiative
- ✓ **Increase of contributory revenue** - impact of 0.2% of GDP
 - 1 p.p. increase of the contribution to the civil servants social security scheme
 - Implementation of the Contributory Code
- **Non tax revenue** - impact of 0.2% of GDP

Privatization Plan

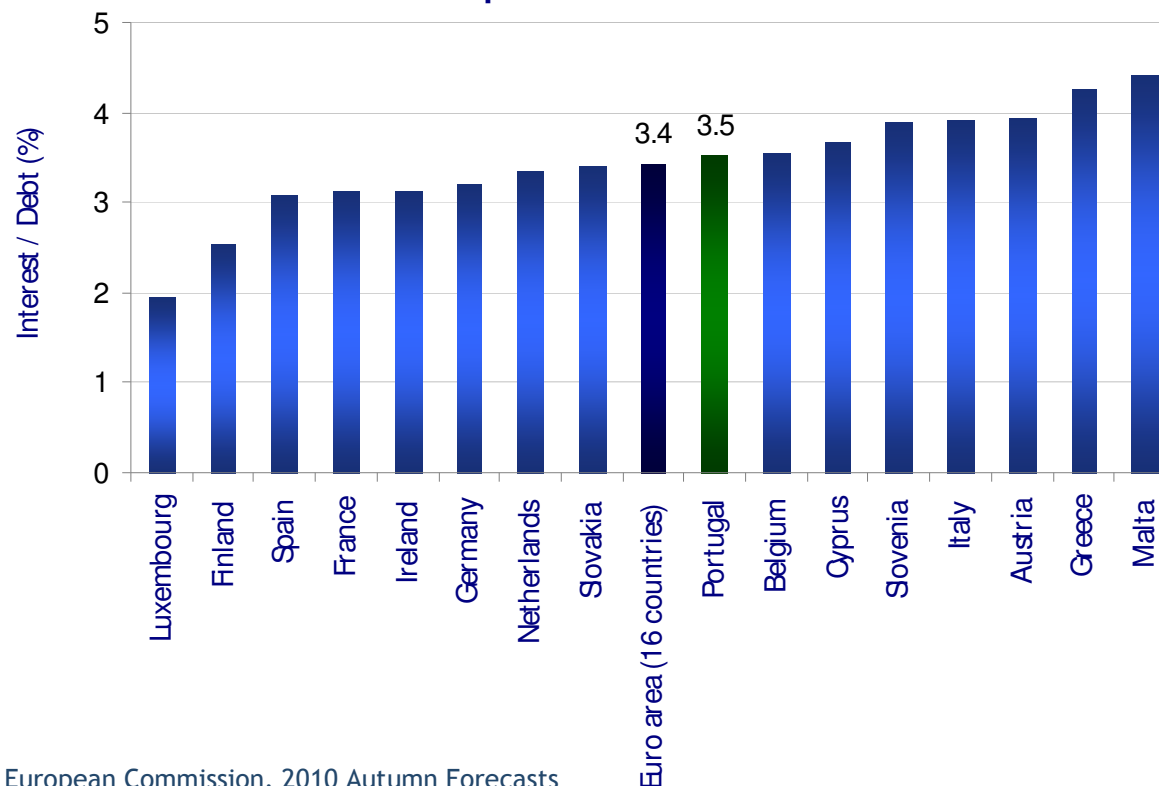
Privatizations of the State-Owned Enterprises, 2010-2013

Company	Sector	Shareholding of the State
Sale of the State's shareholding in full		
BPN	Financial	100%
INAPA – Investimentos, Participações e Gestão, S.A.	Paper	32.7%
Edisoft		60.0%
EID	Defence	38.6%
Empordef TI		100.0%
Sociedade Portuguesa de Empreendimentos SPE. S.A.	Mining	81.1%
Hidroeléctrica de Cahora Bassa, S.A.	Energy	15.0%
Partial sale of the State's shareholding		
GALP Energia, SGPS, S.A.		8.0%
EDP – Energias de Portugal, S.A.	Energy	25.7%
REN – Redes Energéticas Nacionais, S.A.		51.1%
Estaleiros Navais de Viana do Castelo, S.A.	Shipbuilding	100.0%
CP – Carga, S.A.		100.0%
TAP, SGPS, S.A.	Transport	100.0%
CTT – Correios de Portugal, S.A.	Communications	100.0%
ANA – Aeroportos de Portugal, S.A.	Transport	100.0%
Caixa Seguros	Financial	100.0%
EMEF – Emp. de Manutenção de Equip. Ferroviário, S.A.	Transport	100.0%
Concessions		
CP - operation of routes	Transport	100.0%

Between 2010 and 2013 the revenue from privatization is expected to amount to €6,000 million, which will contribute to reduce the General Government debt...

Funding Costs

Debt implicit interest rate in 2010^e



Source: European Commission, 2010 Autumn Forecasts

The Portuguese debt implicit interest rate in 2010 is expected to be in line with the Euro area average.

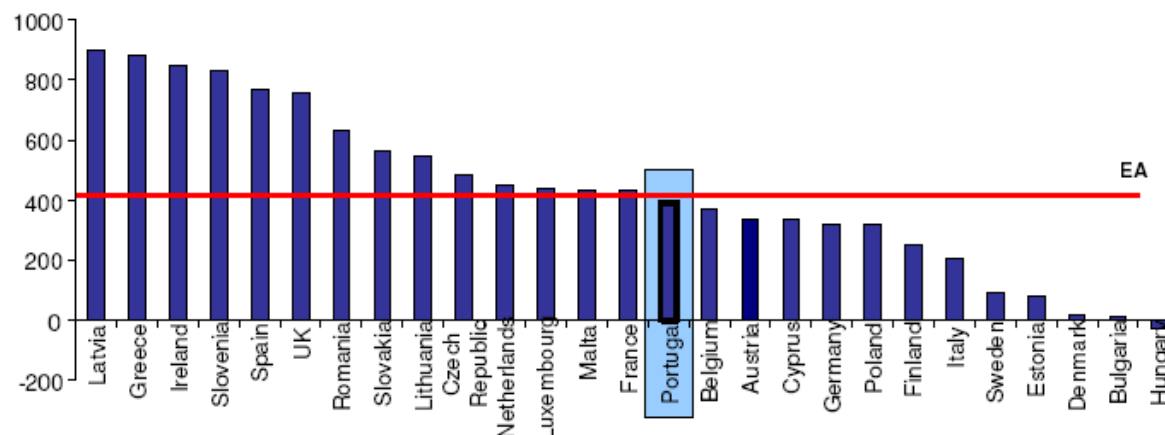
- ✓ In a simulation assuming a very extreme scenario of very high funding costs going forward - 4% on the rollover of the entire T-bill programme and 7% on all bond issuance - Portugal would still have an implicit funding cost below 5% by 2013. This evidences that the country's public finances are quite resilient to the current excessive risk premium on Portuguese debt.

Government Debt

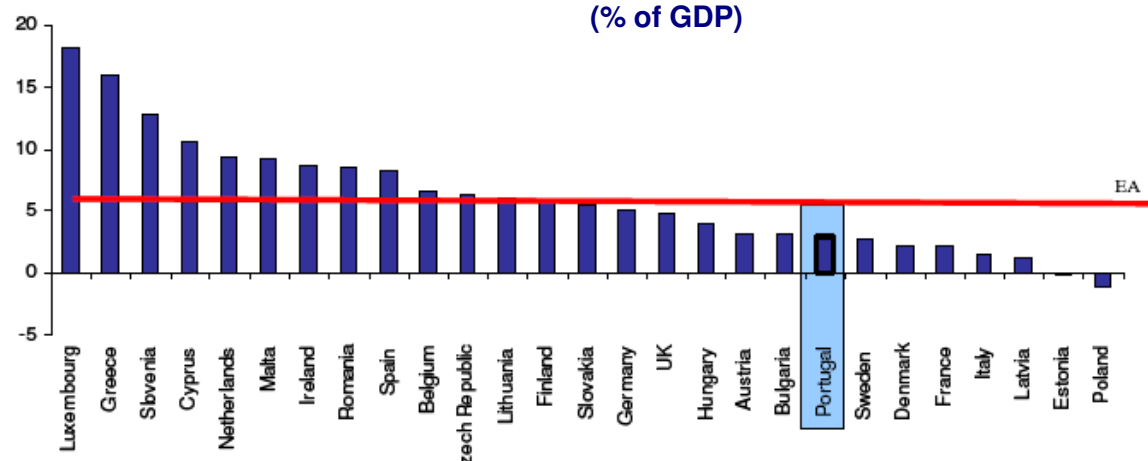
According to the EC 2009 Sustainability Report, Portugal has a more sustainable debt path than the euro area average (due to public pension system reform)...

... and the expected increase in age-related expenditures in Portugal is now one of the smallest in the EU27.

EU27 projected government debt ratio in 2060
(% of GDP)



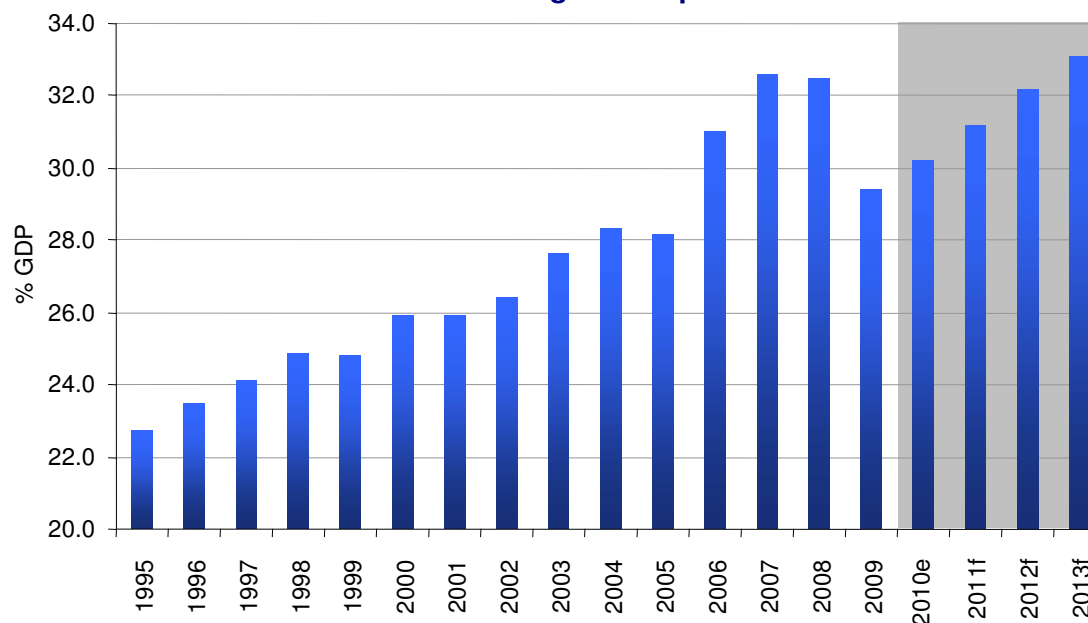
Increase in age-related expenditure, 2010-2060
(% of GDP)



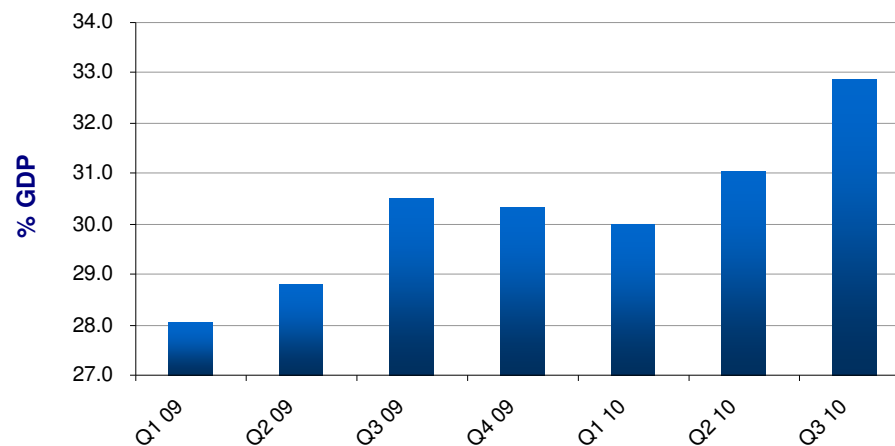
III. Economic Growth Drivers

International Trade

Portuguese Exports



Portuguese Exports (quarterly data)



Source: Statistics Portugal, Ministry of Finance and Public Administration

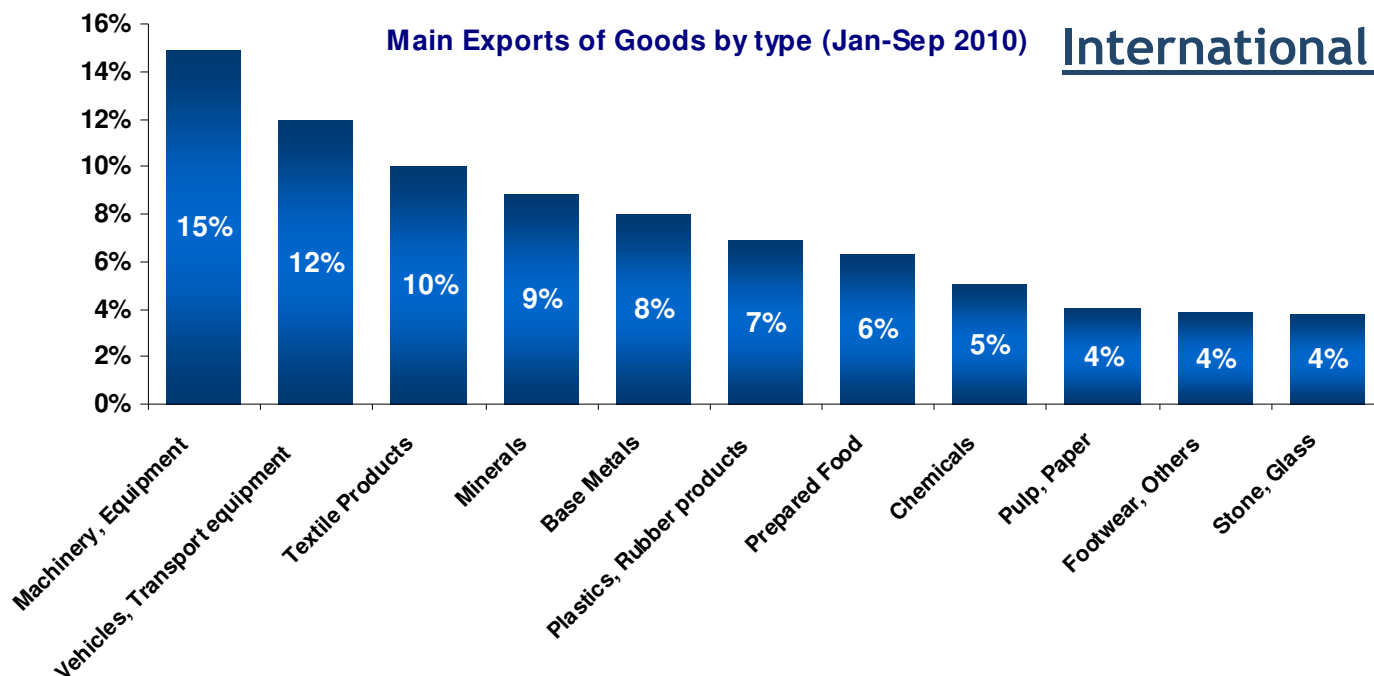
Portuguese exports fell in 2009, in line with international trade but have already started to recover, and this trend is expected to continue in the coming years.

Still relying on traditional trading partners, but increasing exports to a diversified number of markets.

Over the last decade, the share of exports to non-Euro zone countries increased from 15% to 27%.

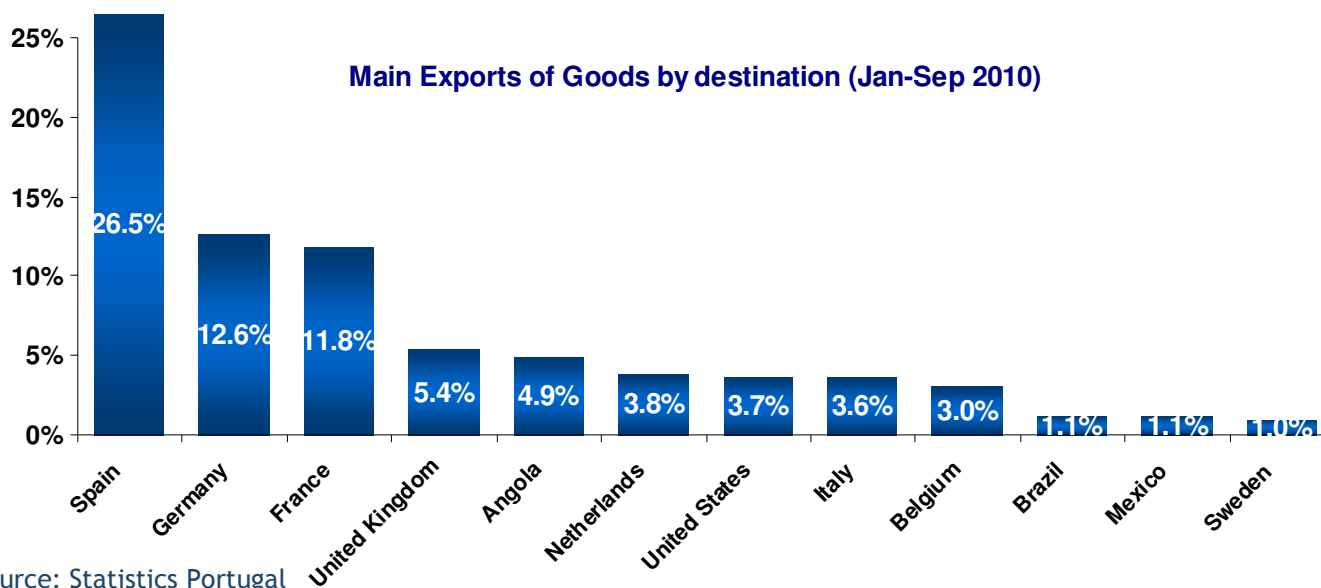
Exports to Spain, Portugal's main trading partner, grew 14.4% (YoY) in Jan-Sep 2010.

Main Exports of Goods by type (Jan-Sep 2010)



International Trade

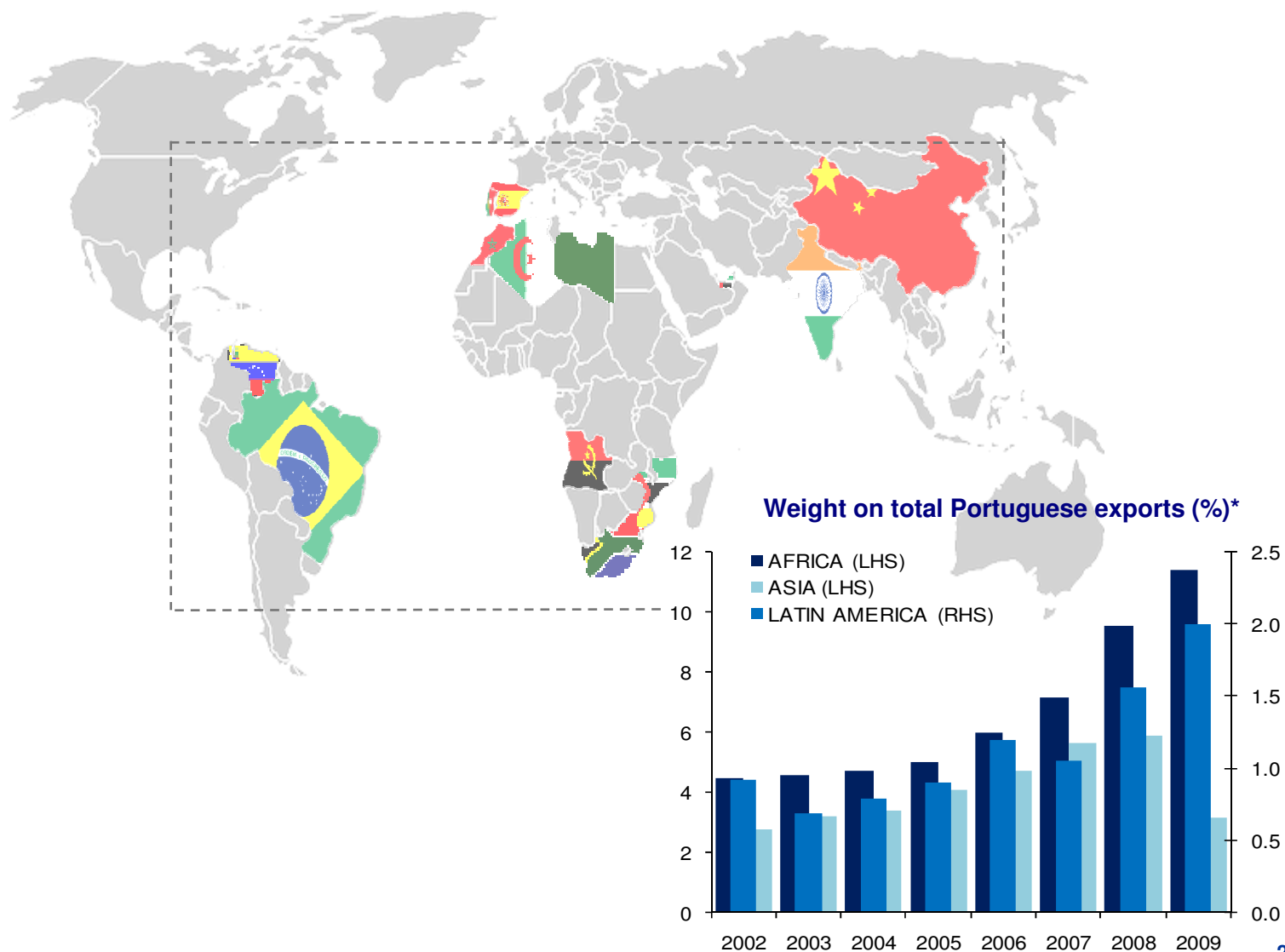
Main Exports of Goods by destination (Jan-Sep 2010)



Source: Statistics Portugal

International Trade

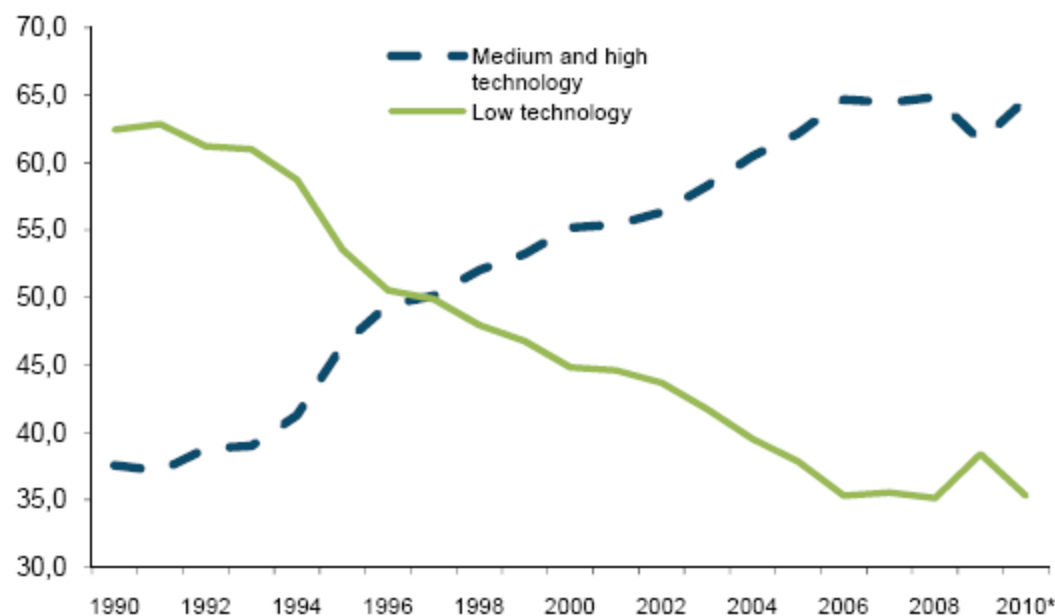
The expansion in the relevant market of the Portuguese economy should provide an important scale effect, supporting exports growth.



Source: INE, Eurostat, ES Research. *Goods.

International Trade

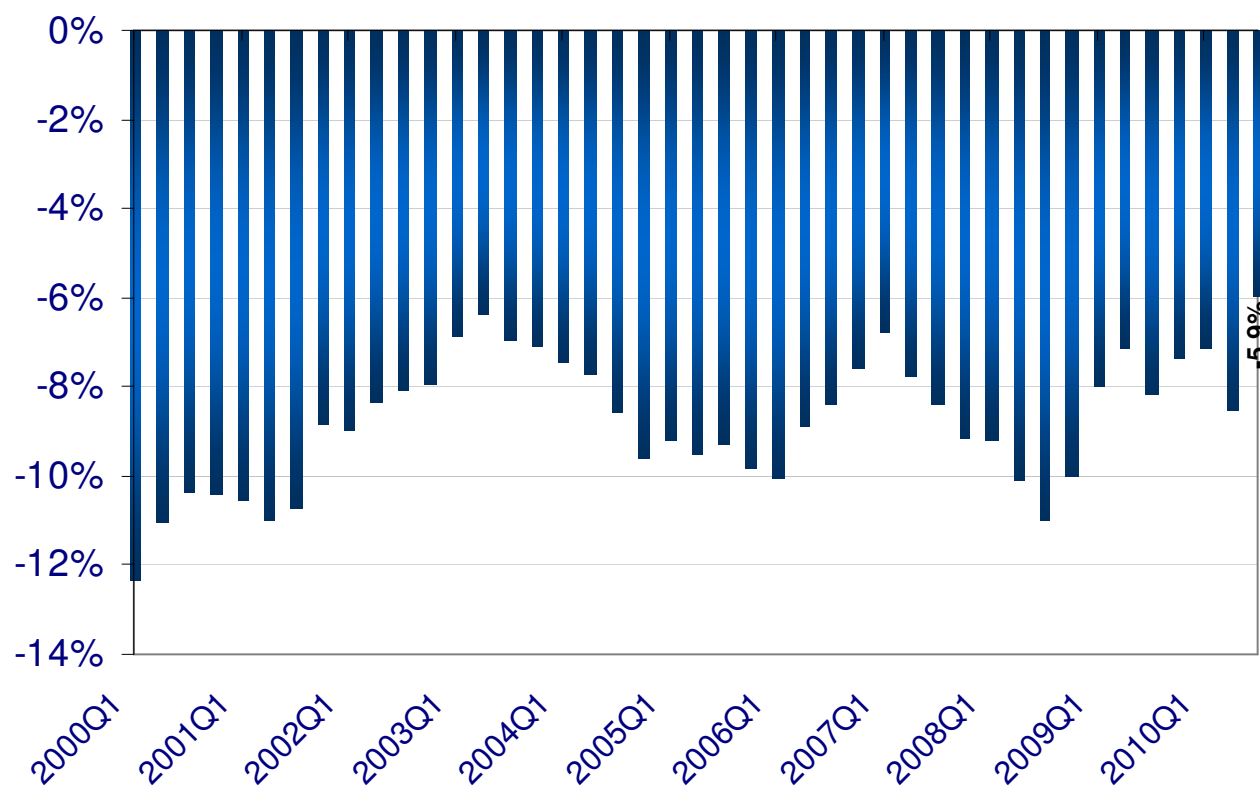
**Technological intensity of Portuguese exports
(% of total)**



Higher value added and higher technological content of exports evidence a positive evolution of the exports profile.

International Trade

**Trade Balance
(% of GDP) - current prices**



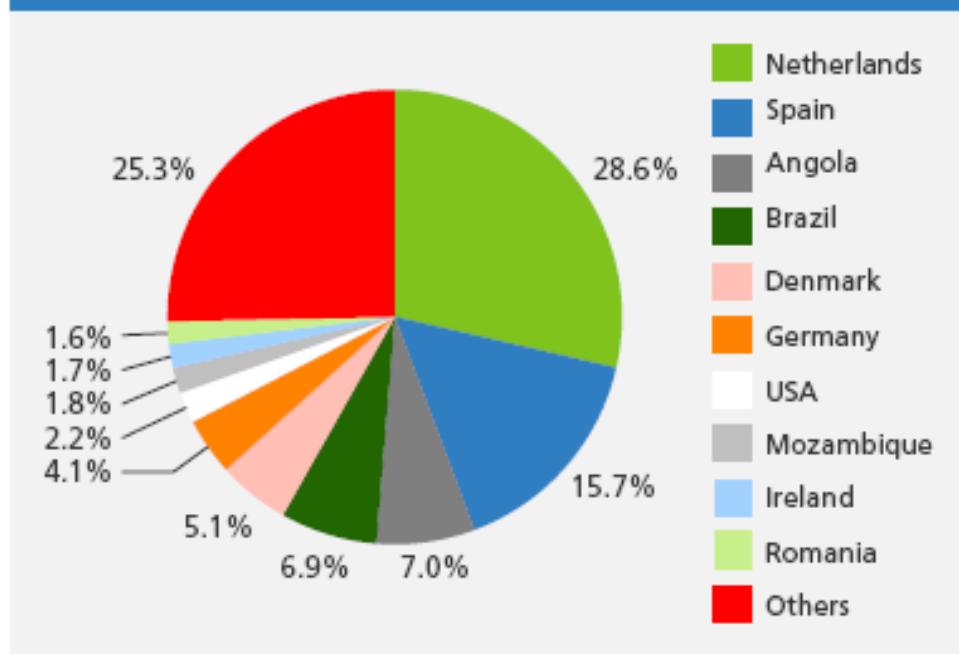
The deficit of the trade balance in the 3rd quarter of 2010 was the lowest of the last 15 years

Internationalization of Portuguese Companies

Portuguese companies' internationalization is well diversified, geographically...

...and almost half of the value of the top 20 listed companies in Euronext Lisbon comes from their international businesses.

Portuguese Foreign Direct Investment by Major Recipients - 2009^a



Source: Bank of Portugal statistical bulletin for March 2010; EUR million;
(a) gross investment

Estimates of PSI-20 enterprise value outside Portugal (% of total)

Altri	97%
Portucel	95%
Sonae Indústria	90%
EDP Renováveis	84%
Semapa	80%
Jerónimo Martins	77%
Cimpor	72%
Galp Energia	60%
EDP	45%
BES	35%
BCP	32%
Portugal Telecom	30%
BPI	30%
Mota-Engil	30%
Sonae	8%
Zon Multimedia	2%
REN	0%
Brisa	0%
Sonaecom	0%
Total	48%

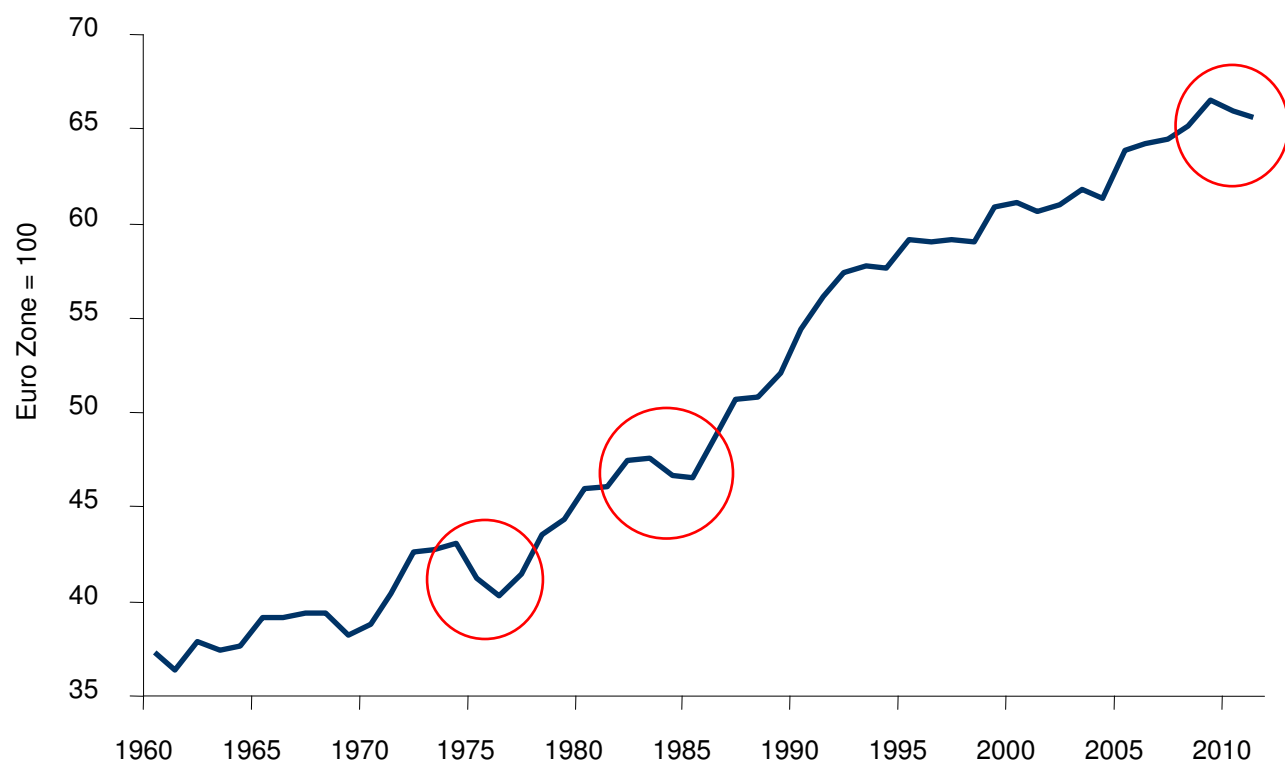
Source: ES Equity Research estimate.

Structural Reforms

Recent divergence in productivity vs. Europe is the main current challenge of the Portuguese economy.

Portugal's long term convergence trend should resume through new structural changes leading to higher productivity growth and competitiveness: lower energy dependency, higher investment in R&D, higher flexibility in labor market, etc.

Labor Productivity (% Euro Area Average, PPP)

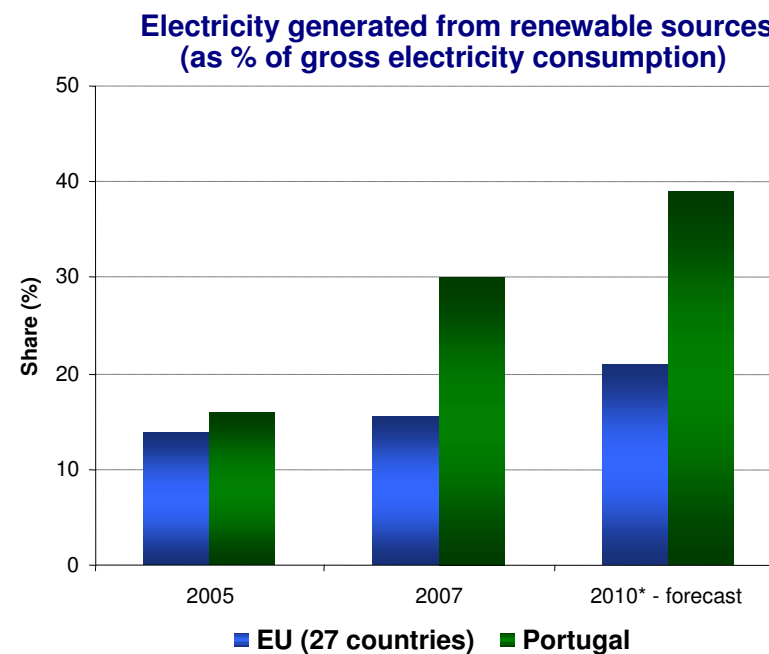
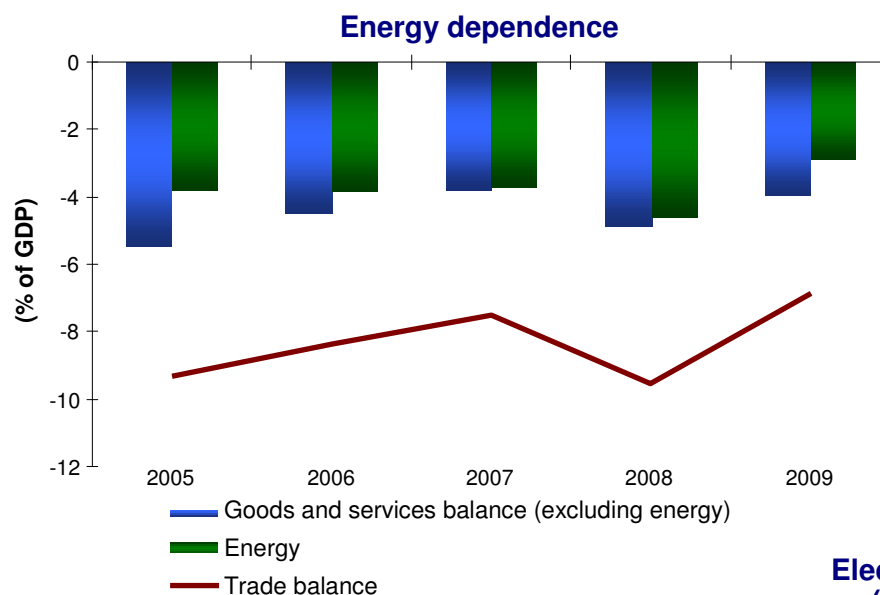


Structural Reforms

The trade deficit problem is largely related to the country's energy dependence.

This is being addressed by the increased use of renewable energy sources.

In 2009, Portugal registered the second largest weight of wind generated electricity in consumption.



Structural Reforms

Main goals of the
National Energy
Strategy 2020

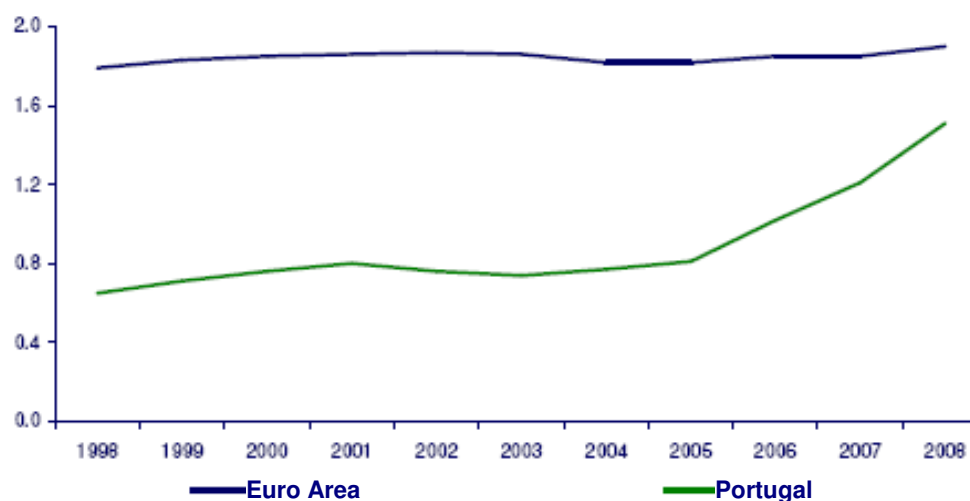
- ✓ Reduction of the country's energy dependence to 74%, from the current 83%
- ✓ 60% of electricity production and 31% of total energy consumption generated from renewable sources
- ✓ 20% reduction in the overall energy consumption
- ✓ 25% reduction on energy imports
- ✓ Promotion of a renewable energy cluster in the Portuguese economy. The weight of the sector is to increase from 0.8% to 1.7% of GDP

Structural Reforms

Investment in R&D is growing, leading to more innovation and new products. Half of this investment comes from the private sector.

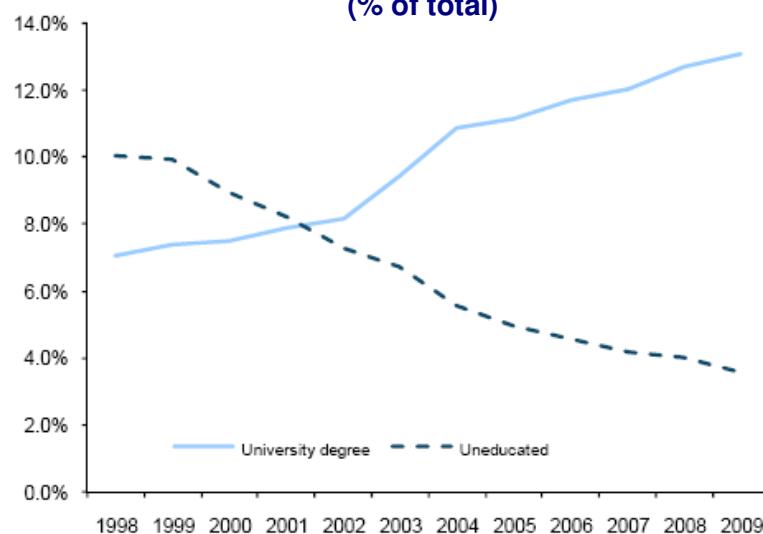
Data for 2009 (Portuguese Ministry of Science, Technology and Higher Education) show an increase to 1.7% of GDP. 2009 data for the Eurozone is still not available.

Portugal: Gross domestic expenditure on R&D (% of GDP)



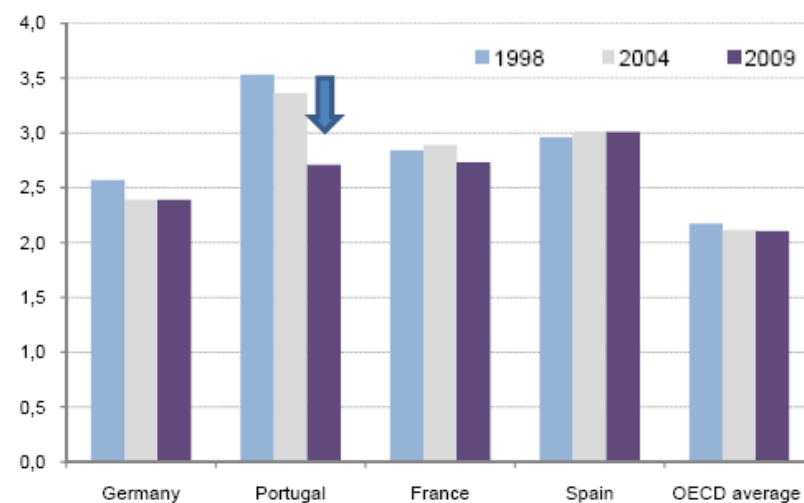
Structural Reforms

Qualification of the Labor Force: University degree and uneducated (% of total)



Source: Statistics Portugal, Ministry of Finance and Public Administration

Labor market rigidity



Source: OECD

Education and labour reforms are already showing results, promoting competitiveness gains.

Structural Reforms

Some of the structural reforms are already showing results.

Portugal currently ranks 24th in the Forbes “Best Countries for Business” (out of 128 countries)...



Special Report
Best Countries for Business
09.08.10, 08:00 PM EDT

RANK	NAME	GDP GROWTH (%)	GDP/CAPITA (\$)	TRADE BALANCE AS % OF GDP	POPULATION (MIL)	FEDERAL BUDGET BALANCE AS % OF GDP
24	Portugal	-2.7	21,700	-10.3	10.7	76.9

Source: Forbes (all economic data from 2009)

...and ranks 31th in the “Ease of doing Business” (out of 183 countries) - Doing Business 2011

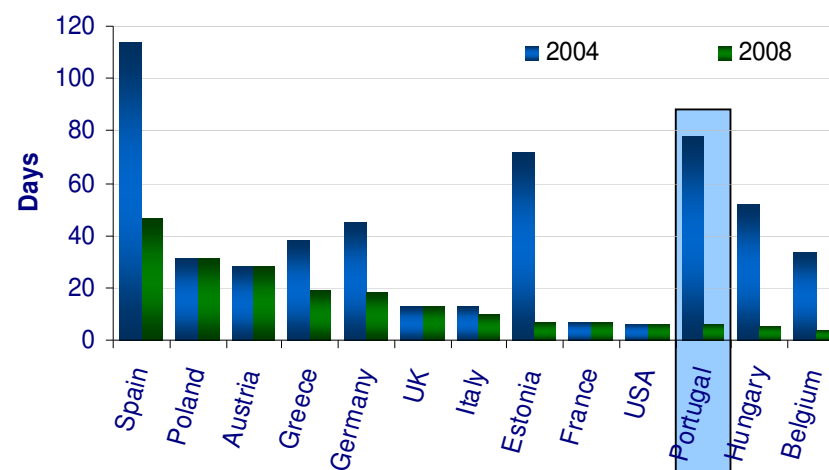
Some of the criteria have improved significantly in the last years.



Rankings on the ease of doing business

DB2011 RANK	DB2010 RANK	ECONOMY	DB2011 REFORMS
31	33	Portugal	2

Starting a Business



Source: Doing Business

IV. Public Debt Management

Issuance Strategy Guidelines

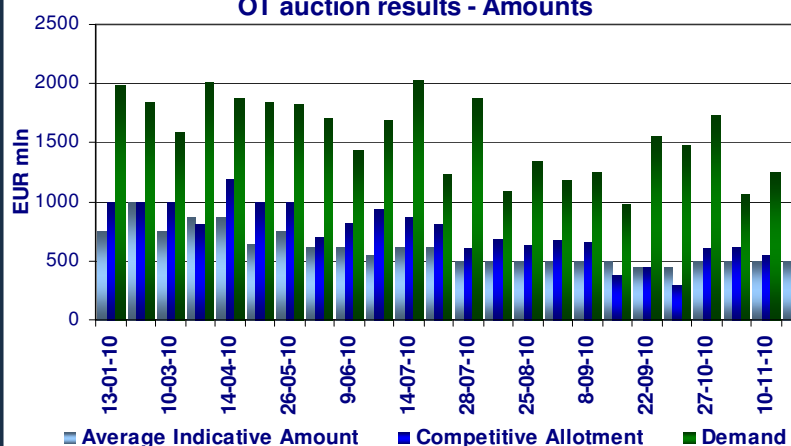
Guidelines on issuance strategy are clear and stable over time, even under particularly challenging market conditions.

- ✓ Market driven borrowing strategy
 - ✓ Primary dealership system, as most countries in the EU
 - ✓ Privileging the increase of liquidity on the curve
 - ✓ Preserving the main pillars of transparency and accountability
 - ✓ Combining predictability with flexibility under challenging market conditions
- ✓ Active debt management
 - ✓ IR swaps to adjust to benchmark duration
 - ✓ Buy-backs to reduce refinancing risk
- ✓ Diversification of Financing Sources and Markets

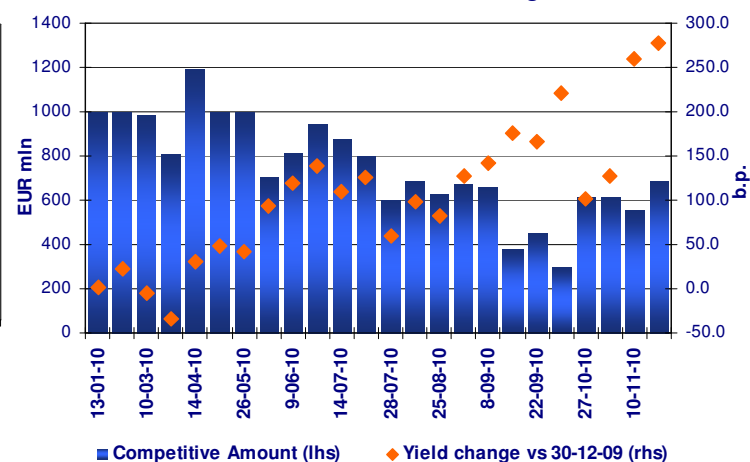
2010 Funding Execution

In 2010, the regular issuing programs (PGB and T-bills) have been met with consistent demand, even if at higher yields, particularly since May.

OT auction results - Amounts

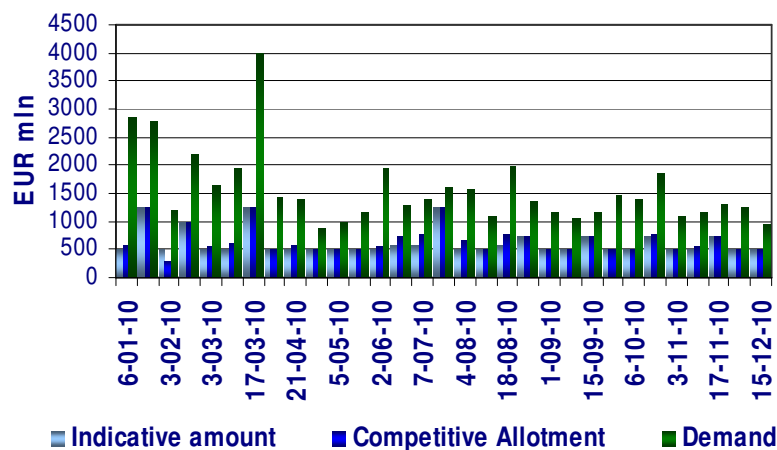


OT auction results - Yield Change

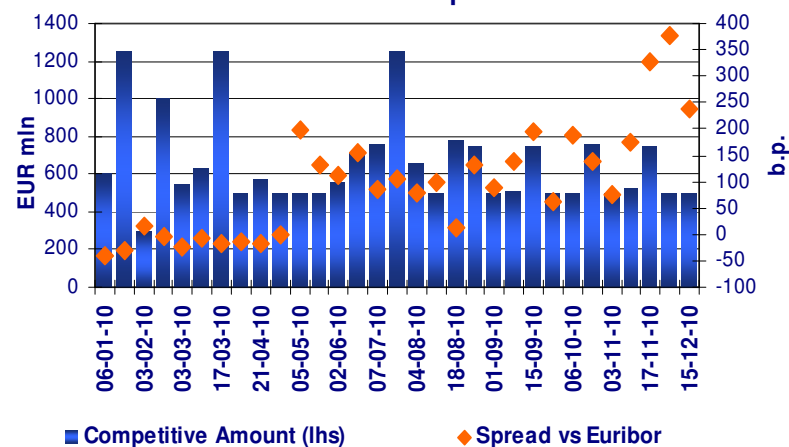


*In the PGB 2020 yield change, the OT2019 yield on Dec 30th was used as a reference.

BT auction results - Amounts

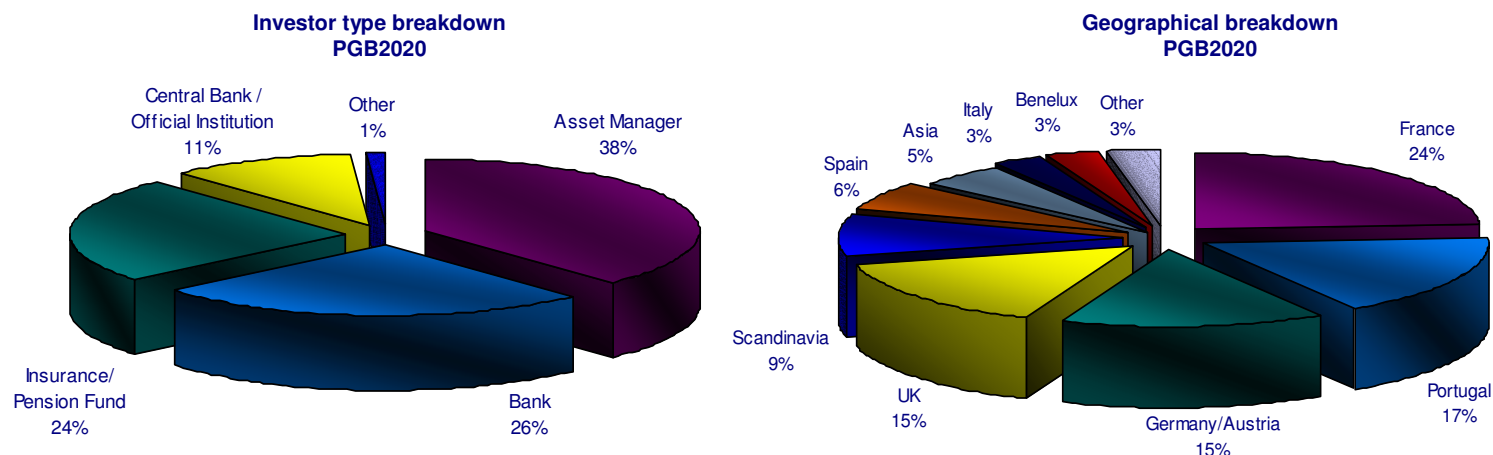


BT auction results - Spread vs Euribor

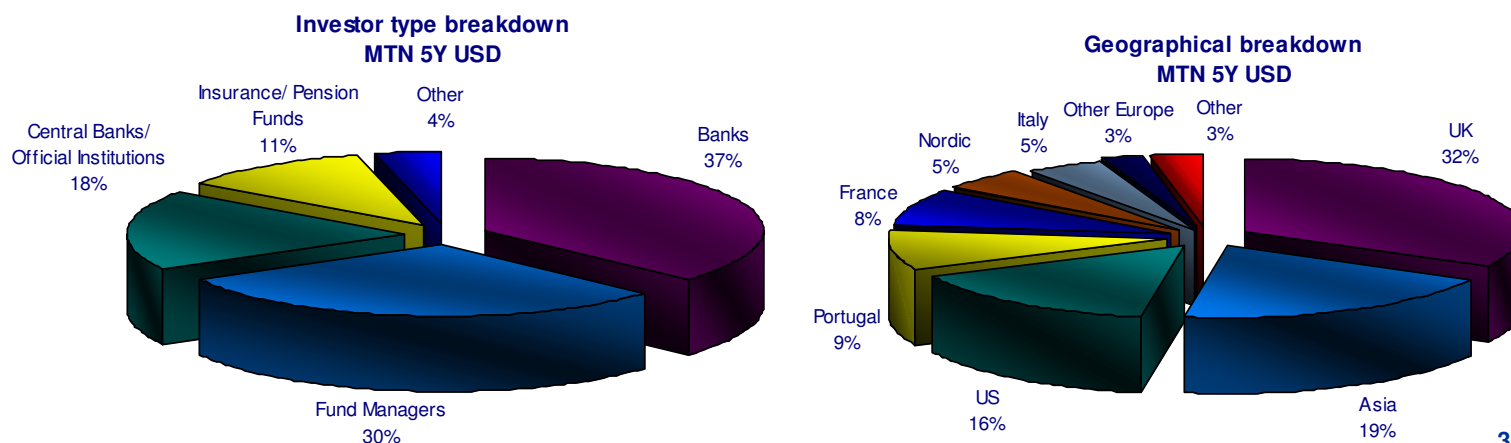


2010 Funding Execution

✓ Syndicated issuance of the new 10Y benchmark



✓ Inaugural syndicated issuance of the USD benchmark (MTN program)



Source: IGCP

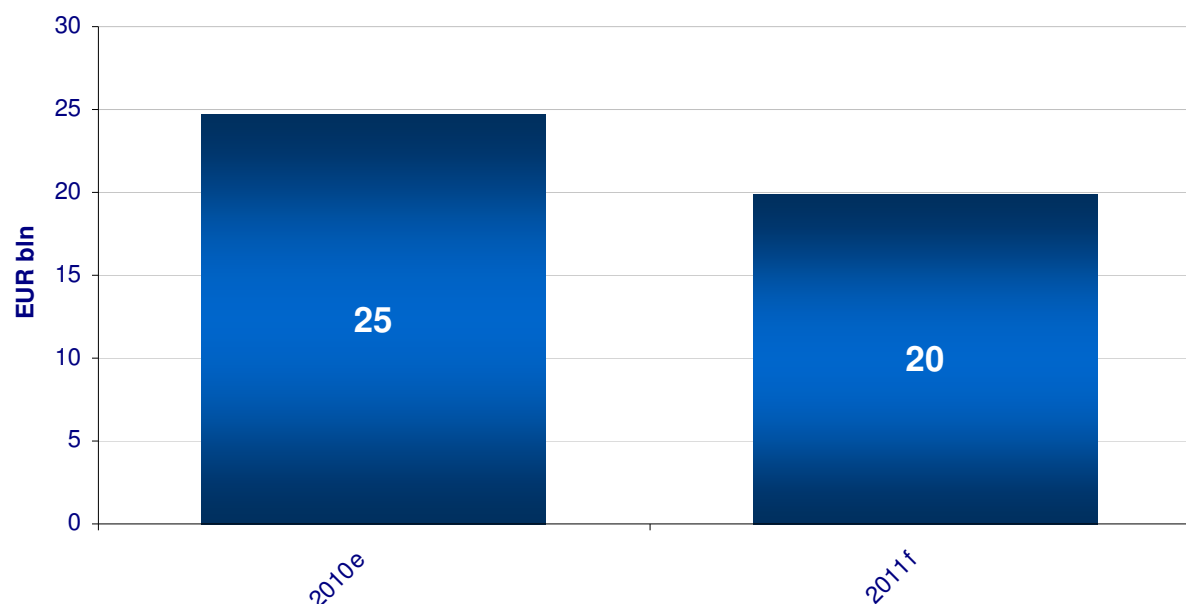
Two syndicated deals in 2010, both well distributed geographically and by investor type.

Launch of USD benchmark (MTN programme) increased the reach to investors in Asia and the US, and also contributed to a larger allocation to Central Banks.

2011 Funding Programme

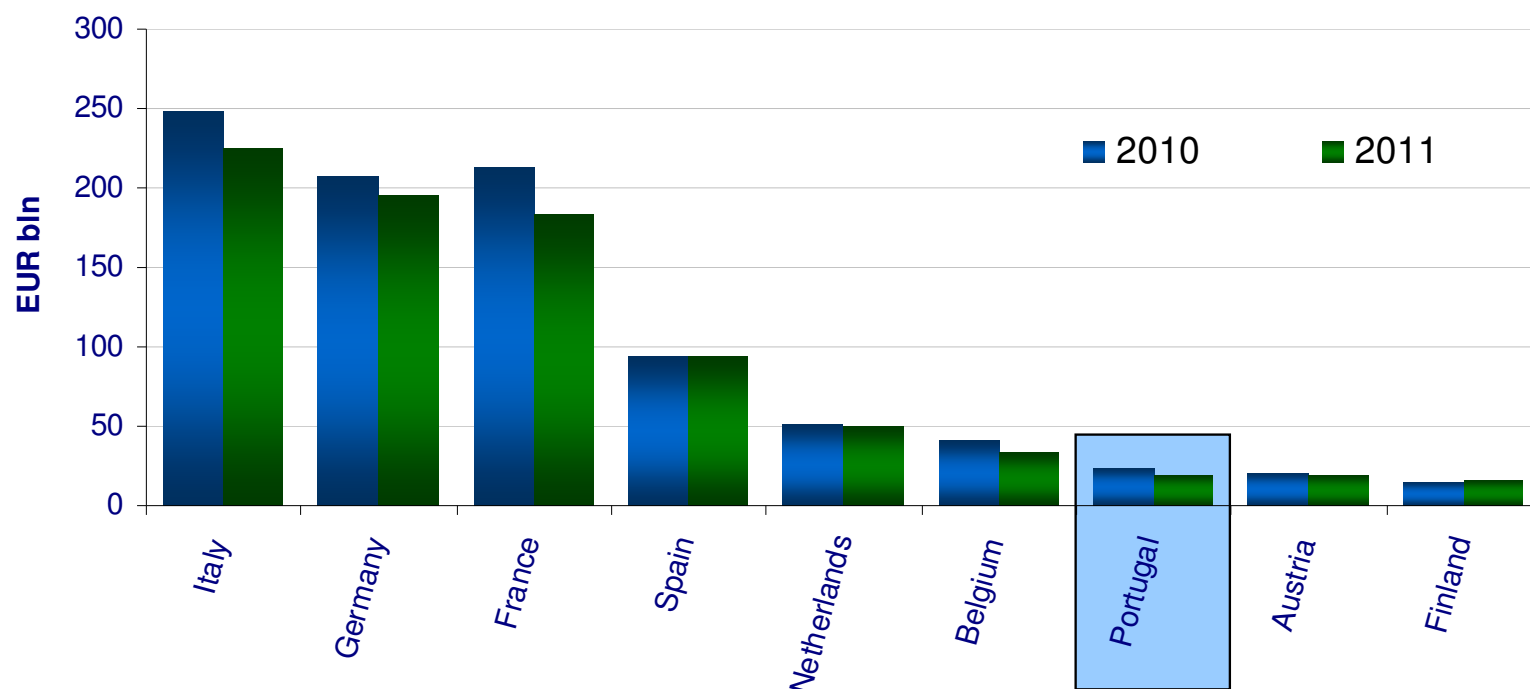
The forecasted gross funding for 2011 is EUR 5 bln lower than in 2010.

Gross Funding



2011 Funding Programme

Medium and long-term funding



The 2011 Portuguese Funding Programme estimates bond issuance of EUR 18 to 20 bln, which is relatively low when compared with most other Euro Area sovereigns - scarcity value

2011 Funding Programme

- ✓ Borrowing needs: around EUR 20 billion
- ✓ OT issuance: EUR 18 to 20 billion
 - Launch of 1 or 2 new benchmarks
 - Reopening of new lines and off-the-run (through auctions of 1 or 2 lines)
 - Maximum outstanding of EUR 10 bln (per line)
- ✓ BT net issuance: marginally positive, with the launch of ten new lines
- ✓ Focused on minimizing the debt cost in a long-term perspective and non exposure to excessive risks
- ✓ MTN issuance on an opportunistic basis and also to reach new investors
- ✓ Other short term funding sources can also be used (such as repos, credit facilities and commercial paper)

Main topics of the
2011 Funding
Programme

2011 Funding Programme

Subject to market conditions, the guidelines for the first quarter of 2011 are:

- ✓Launch of a new syndicated OT series
- ✓Tap of 4 to 6 OT series, via auction
- ✓Hold the following BT auctions:

Instrument	Type	Indicative date	Indicative amount EUR million
BT22JUL2011	Reopening (6 months)	5-Jan-11	500
BT20JAN2012	Launch	19-Jan-11	750-1,250
BT19AGO2011	Reopening (6 months)	2-Fev-11	750-1,500
BT20JAN2012	Reopening (12 months)	2-Fev-11	
BT17FEV2012	Launch	16-Fev-11	750-1,250
BT23SET2011	Reopening (6 months)	2-Mar-11	750-1,500
BT17FEV2012	Reopening (12 months)	2-Mar-11	
BT23MAR2012	Launch	16-Mar-11	750-1,250

Planned issuance for
the first quarter of
2011

2011 Funding Programme

The execution of the funding programme for 2011 is proceeding according to plan, and over EUR 4 bn have already been raised.

Auction Date	Instrument	Amount (EUR mln)*	Average Yield	bid-to-cover
05/01/11	BT 22JUL2011	541	3.686%	2.6
12/01/11	OT 3.6 OCT 2014	691	5.395%	2.6
	OT 4.8 JUN 2020	648	6.717%	3.2
19/01/11	BT 20JAN2012	1017	4.029%	3.1

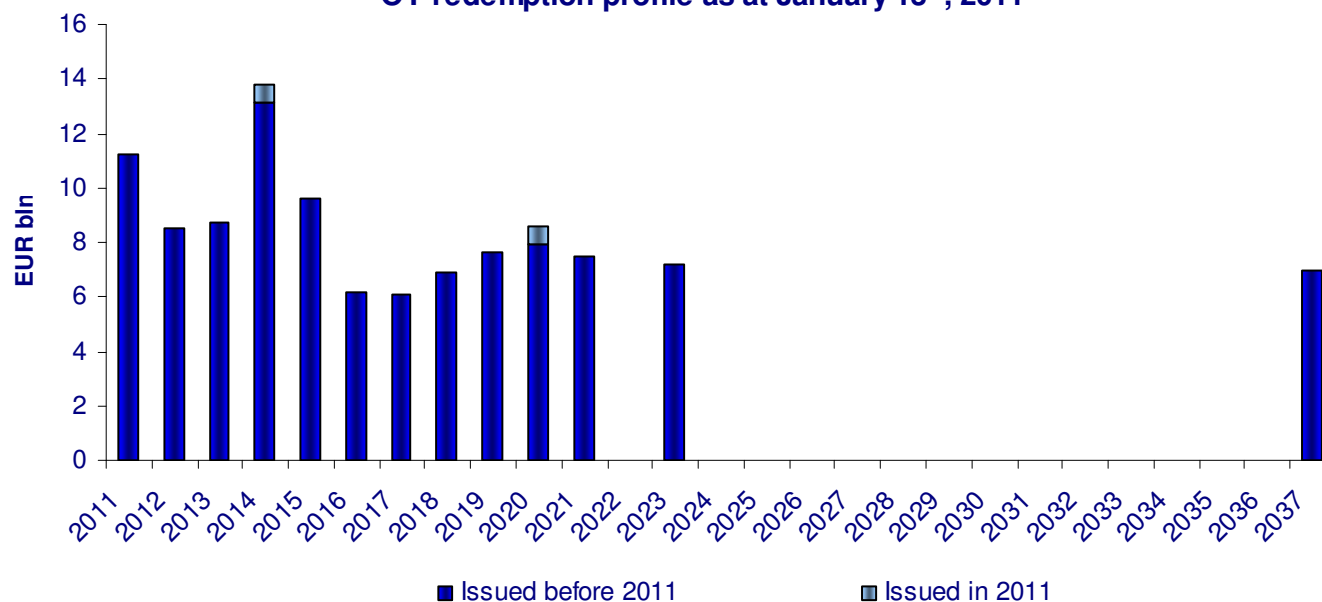
* including non-competitive allocation

Trade Date	Maturity	Amount (EUR mln)
05/01/11	July 2012	1000
07/01/11	January 2021	50
18/01/11	January 2013	110

Funding execution
up-to-date

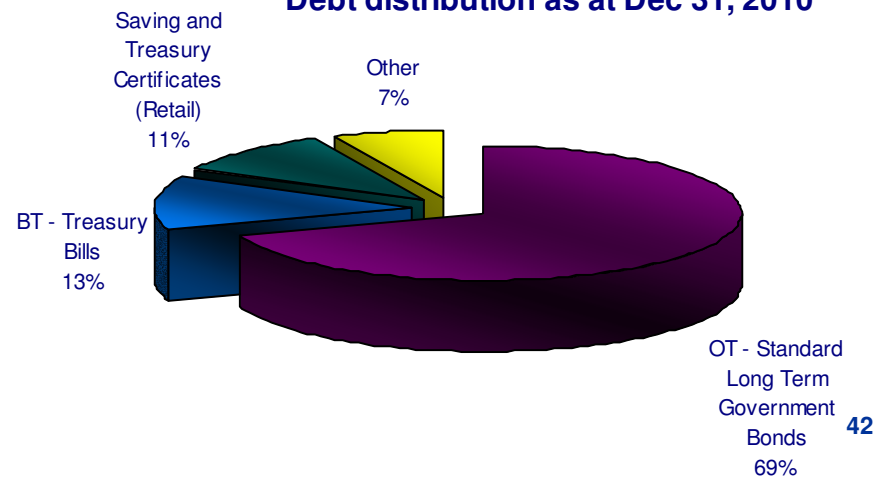
2011 Funding Programme

OT redemption profile as at January 13th, 2011



•PGB represent 69% of total outstanding debt

Debt distribution as at Dec 31, 2010

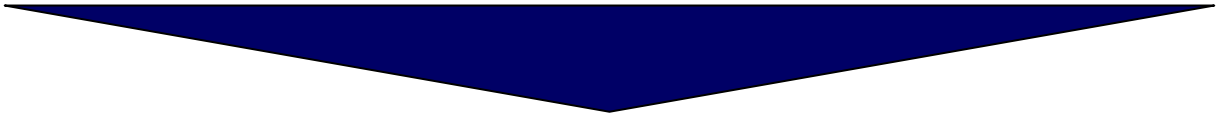


Source: IGCP

V. Wrap Up

Wrap Up

- ✓ Portugal is suffering contagion effects
- ✓ Broad political and social consensus on the need to pursue the consolidation of public finances with a significant austerity package in the 2011 budget
- ✓ Regaining market confidence and normalizing the economy's access to external funding are the main priorities
- ✓ Structural reforms already implemented will produce results in the medium term
- ✓ Stronger activity growth should come from structural reforms and from the expansion to fast growing emerging economies in the South Atlantic



Current risk premium on Portuguese debt offers an excellent investment opportunity

Appendix

RoP Ratings

<i>Agency</i>	<i>Rating</i>	<i>Since</i>	<i>Outlook</i>	<i>Action</i>
Standard & Poor's	A-	Apr-10	Creditwatch Negative	Nov-10
Moody's	A1	Jul-10	Review for possible downgrade	Dec-10
Fitch ratings	A+	Dec-10	Negative	Dec-10

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Web site: igcp.pt

Reuters pages: IGCP01

Bloomberg pages: IGCP

Further information on the Portuguese economy can be obtained from:

The Office of Planning, Strategy, Assessment and International Relations

www.gpeari.min-financas.pt

Budget Department

www.dgo.pt

Statistics Portugal

www.ine.pt

Banco de Portugal (Central bank)

www.bportugal.pt

Further information on the Portuguese secondary market can be obtained from:

MTS Portugal:

http://www.mtsmarkets.com/Products/~media/MTS/Available_Markets/Portugal.pdf

Reuters pages: PT/MTS1